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ABSTRACT

The Telecommunications Act of 1996 expanded universal support to eligible schools and libraries. To administer the universal service program for schools and libraries, the Federal Communications Commission (FCC) directed the creation of the Schools and Libraries Corporation (Corporation). As a start-up operation, the Corporation has had to develop operating procedures and internal controls to implement FCC's orders guiding the program. This testimony focuses on issues related to the Corporation's operating procedures and internal controls, including: its progress in reviewing applications; the scope and timing of key compliance tests; and the status of the independent audit to determine whether the Corporation has developed an appropriate set of internal controls to mitigate against fraud, waste, and abuse. The testimony also discusses FCC's efforts to establish strategic goals and performance measures for the schools and libraries program, as required by the Government Performance and Results Act of 1993. Overall, the review of the Corporation's activities to date indicated that it has made substantial progress in establishing an operational framework for the program that is consistent with relevant FCC orders. The several areas of concern that were identified are discussed, results of the audit work are detailed, and recommendations for strengthening the Corporation's internal controls are given. (AEF)

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SCHOOLS AND LIBRARIES CORPORATION

Actions Needed to Strengthen Program Integrity Operations Before Committing Funds

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Mr. Chairman and Members of the Committee:

We are pleased to be here today to discuss the implementation of the new universal service program for schools and libraries. As you know, the Telecommunications Act of 1996 expanded universal support to eligible schools and libraries. The general purpose of this program is to improve the access of schools and libraries to modern telecommunications services. To meet this goal, schools and libraries would receive discounts on the costs of services provided by vendors.

To administer the program, the Federal Communications Commission (FCC) directed the creation of the Schools and Libraries Corporation (Corporation). As a start-up operation, the Corporation has had to develop operating procedures and internal controls to implement FCC's orders guiding the program. This includes informing potential applicants about the program, establishing application procedures, processing and reviewing applications, and authorizing the disbursement of funds to vendors providing eligible services to the applicants.

At your request, Mr. Chairman, we reviewed the Corporation's activities to date. Our testimony today will focus on issues related to the Corporation's operating procedures and internal controls, including:

- its progress in reviewing applications;
- the scope and timing of key compliance tests;
- the status of its efforts to finalize its operating procedures; and
- the status of the independent audit to determine whether the Corporation has developed an appropriate set of internal controls to mitigate against fraud, waste, and abuse.

Our testimony will also discuss FCC's efforts to establish strategic goals and performance measures for the schools and libraries program, as required by the Government Performance and Results Act of 1993.

Overall, we found that the Corporation has made substantial progress in establishing an operational framework for the program that is consistent with relevant FCC orders. However, we identified several areas of concern, discussed below.

With regard to processing applications, the Corporation has worked with schools and libraries to inform them about the program and its application procedures. During the initial application period, which began on

January 30, 1998, and ended on April 15, 1998, schools and libraries sent in over 32,600 applications for discounts. On the basis of a sample of applications submitted, the Corporation estimates that about $2 billion in discounts for telecommunications, Internet services, and internal connections have been requested. However, processing these applications has taken longer than either the Corporation or FCC expected. They both hoped to have this activity completed in time to make funding commitments to applicants by the end of June 1998. As of last week, only about 62 percent of the applications have been processed and entered into the Corporation's database.

The Corporation relies on a combination of applicants' self-certifications, third-party reviews, and its own procedures to ensure compliance with FCC's rules and regulations. The Corporation tests applications for compliance with rules on the eligibility of applicants and requested services, and on the amount of requested discounts. However, the same test criteria have not been applied to all the applications because the criteria have changed over time. Also, while the Corporation plans to conduct additional tests and reviews to ensure that applications are consistent with program rules, their scope and timing have not been finalized. Reviews of high-risk applications are not scheduled to occur until sometime after funding commitment letters have been sent to applicants. Should the Corporation find major problems at this time with the applications reviewed, it may have to reduce or withdraw funding commitments from applicants. If such applicants have already begun receiving services on the basis of their commitment letters, they might find themselves responsible for paying a higher cost for those services than they planned.

While the Corporation has established procedures for initially reviewing the applications, it has not yet finalized all necessary procedures and related internal controls for the program. In particular, the Corporation is still developing the processes and controls for notifying applicants of the amounts of their approved discounts and for authorizing distribution of funds to vendors to cover discounted services that they provide to schools and libraries. We are particularly concerned about this because the Corporation estimates that invoices for payment could begin to arrive as soon as 15 days after commitment letters are sent out. If disbursement procedures and internal controls are not in place when commitment letters are issued, the Corporation may find itself unable to process vendor invoices in a timely manner.

The FCC Chairman has called for an independent audit of the Corporation's internal controls to help mitigate against fraud, waste, and abuse. The audit report is scheduled to be completed before funds are disbursed, but not before funds are committed to applicants and their vendors. Since applicants and vendors could begin submitting forms and invoices for disbursement of funds as soon as 15 days after they receive their commitment letters, it is important that the Corporation have all of its disbursement procedures, systems, and controls in place and reviewed by the independent auditor before sending these letters. If the auditor's final report is not received until after commitments are made and the report identifies problems with disbursement procedures, it may be difficult for the Corporation to resolve them in a timely manner so that vendor invoices can be processed promptly and accurately.

Finally, FCC has not developed performance goals and measures for this program consistent with the requirements of the Government Performance and Results Act of 1993. FCC's "Strategic Plan for Fiscal Years 1997-2002 and Annual Performance Plan for Fiscal Year 1999" mentions the schools and libraries program in the context of a large number of telecommunications initiatives, but establishes no specific performance measures or target levels of performance to be achieved by the program.

We should note, Mr. Chairman, that the Corporation is still developing and finalizing some of its procedures and controls, and that they are subject to change. For example, the Corporation is currently faced with the task of implementing procedural changes in response to changes in the program made recently by FCC. In addition, Corporation officials are currently considering changes to procedures and internal controls aimed at addressing concerns that we raised with them during our review.

We will now go into more detail about the results of our audit work to date and present our recommendations for strengthening the Corporation's internal controls.

Background

Traditionally, "universal service" has meant providing residential customers with affordable, nationwide access to basic telephone service. The Telecommunications Act of 1996, among other things, extended universal service support to eligible schools and libraries. The Act also specified that every telecommunications carrier that provides interstate telecommunications services, unless exempted by FCC, must contribute to a universal service fund. Finally, the Act directed FCC to convene a

federal-state Joint Board to specify which services should be supported by the federal universal service mechanisms and recommend regulatory changes to provide such support.

In its May 1997 universal service order, FCC adopted the Joint Board's recommendation that eligible schools and libraries could receive discounts of between 20 to 90 percent on all telecommunications services, Internet access, and internal connections, subject to a $2.25 billion annual cap.[1] Changes have been made to the program through a number of reconsideration orders, the latest of which was released on June 22, 1998. These orders define the size, time frame, and eligibility requirements for the schools and libraries program, the type and level of funding support available from universal service funds, and the administrative structure of the program, among other things.

The general purpose of this program is to improve the access of schools and libraries to modern telecommunications services. Generally, any school that meets the Elementary and Secondary Education Act of 1965's definition of schools is eligible to participate,[2] as are libraries that can receive assistance from a state's library administrative agency under the Library Services and Technology Act.[3] In addition, the orders specifically define the three classes of services that are eligible for universal service support: telecommunications services, Internet access, and internal connections.

FCC has defined the mechanism by which eligible schools and libraries will receive support from the universal service program. Specifically, schools and libraries do not receive direct funding from the program. Instead, they receive discounts on the costs of services provided by vendors. The amount of discount each school or library can receive under the program ranges from 20 to 90 percent and is determined using a matrix designed by FCC, with schools and libraries located in rural and low-income areas receiving the highest discounts from the fund.[4] The universal service fund

[1]FCC's universal service order has been challenged in Federal court. Texas Office of Public Utility Counsel v. FCC, No. 97-60421 (5th Cir. filed June 25, 1997).

[2]Examples of entities not eligible to receive universal service support are home school programs, institutions of higher education, and private vocational programs.

[3]Libraries whose budgets are part of a school's budget are not eligible to receive universal service support.

[4]The program measures how economically disadvantaged the schools and libraries are by the number of students eligible to participate in the national school lunch program. Urban and rural designations are based on the Metropolitan Statistical Area (MSA) listing.

compensates the schools' and libraries' vendors for the amount of the discounts.

The act did not prescribe a structure for administering the program. However, the FCC directed the establishment of the Schools and Libraries Corporation. FCC's Chairman selects or approves the Corporation's Board of Directors as well as the hiring and removing of the Chief Executive Officer. Under FCC's orders, the Corporation is responsible for administering certain functions of the program, including processing and reviewing the applications and administering an Internet site on the World Wide Web. FCC also specified that the Corporation can only engage in activities that are consistent with FCC orders and rules.

FCC's latest reconsideration order significantly changed the program. Specifically, this order changed the funding year from a calendar year cycle to a fiscal year cycle and extended the first funding round period to 18 months. The order also adjusted the maximum amounts that could be collected and spent during 1998 and the first 6 months of 1999 and directed the Corporation to commit no more than $1.925 billion for the schools and libraries support program during this time frame. FCC also directed the Corporation to fund requests for telecommunication and Internet services first and then fund requests for internal connections. Those applicants eligible for the highest levels of discounts would receive funding priority for internal connections.

Structure of the Schools and Libraries Corporation

The Corporation currently has 15 staff, all based in Washington, who manage the application and disbursement process and conduct outreach to potential applicants. To date, the Corporation has conducted over 130 outreach sessions informing schools and libraries about the program. In addition, the Corporation has established a web site that contains program applications, information, and updates. The Corporation also has provided training to its contractors' staff in answering applicants' questions and processing and reviewing applications.

The Corporation has contracted out most of the application-processing, client support, and review functions to the National Exchange Carrier Association (NECA).[5] NECA has 66 staff, the majority of whom are part of the program integrity assurance operation, which reviews the applications for compliance with the program's eligibility requirements.

[5]NECA was established at FCC's direction in 1983 to administer interstate access tariffs and the revenue distribution process for local telephone companies.

NECA has also subcontracted with two organizations to provide customer support, process and enter the applications into the Corporation's database, and establish and maintain the Corporation's web site. As of June 1998, these two subcontractors employed approximately 390 staff dedicated to Corporation activities. According to Corporation officials, however, the subcontractors' staffing levels could decrease as the system designs are finalized and the number of applications needing processing declines.

The Corporation was established in the Fall 1997. The Corporation stated that its operating expenses for calendar year 1997 were approximately $1.9 million. For calendar year 1998, the first full year of program operations, the Corporation estimates its operating expenses at $18.8 million. Most of this estimate covers the costs of contracts, including the Corporation's contract with NECA and an independent auditor. Corporation staff stated, however, that the 1998 estimate may increase as program procedures and systems need to be redesigned in response to FCC's recent rule changes.

Processing of Applications Is Taking Longer Than Expected

To receive universal service support, schools and libraries must complete a two-stage application process which, for the program's first year of funding, began in January 1998. During the first stage, applicants post requests for services on the Corporation's web site so that vendors can provide the applicants with bids on the cost of providing the requested services. The Corporation has received to date nearly 48,000 of these initial applications (FCC Form 470).

The second stage of the process begins after the schools and libraries have accepted a bid and entered into a contract with a service vendor. The applicants then submit on paper a second application (FCC Form 471) that details the types and costs of the services being contracted for, and the amount of the discount being requested. In its original order, FCC determined that applications would be funded on a first-come, first-served basis. Subsequently, FCC amended its rules and the Corporation established a 75-day window within which these second applications would be considered as arriving at the same time. This was done, in part, in order to reduce disparities between applicants with substantial administrative resources and applicants with fewer resources. As a result, the applications received within this window are not funded on a first-come, first-served basis. Approximately 32,600 applications were

received during this initial window. The Corporation estimates that the applications contain approximately $2 billion in requests for discounts.

The Corporation's contractors review the second applications for compliance with what the Corporation considers to be "minimum processing standards," which include a check for original signatures, completeness, and legibility. If the minimum standards are not met, the application is rejected. If the standards are met but other problems with the application are found, the application is sent to a problem resolution team that contacts the applicant to make corrections. After these problems are corrected, information from the application is entered into a database.

FCC and the Corporation anticipated that all of the first year's applications would be processed by the end of June 1998. According to the Corporation, however, as of July 7, 1998, information from only about 20,400 of the 32,600 applications (about 62 percent) received within the initial window had been entered into the Corporation's database. Of the remaining applications, approximately 2,560 (8 percent) were rejected for not meeting minimum processing standards, 1,600 (5 percent) are in problem resolution, and 7,900 (24 percent) applications are awaiting data entry.[6]

According to Corporation officials, the delay occurred because the contractors have had to spend more time than expected in working with applicants to resolve problems. The officials stated that applicants found some parts of the applications and instructions confusing. In addition, the officials noted that the contractors made some mistakes initially in applying the minimum processing standards. Therefore, some rejected applicants are currently being contacted to resolve their problems, enter their data, and place them back in the initial application window.

Concerns Over Key Compliance Checks

To ensure compliance with FCC rules and regulations, the Corporation relies on a combination of applicants' self-certifications, third-party reviews, and its own procedures. Applicants are required to self-certify that they are following the program's rules, and third parties, such as state-level education and library agencies, certify that the schools and libraries have technology plans in place that show how technology will be used to support their educational goals. In addition, the Corporation's staff and contractors check applications to ensure that applicants are eligible,

[6]Approximately 140 applications have been withdrawn.

services are eligible, and discount levels are appropriate. The way the Corporation is conducting key compliance tests, however, raises our concern about how effective the tests will be in detecting deviations from program rules.

We are also concerned about the timing of detailed reviews that the Corporation plans to conduct on a set of applications judged to be "high risk," to provide further assurance that program rules are being followed. Currently, the Corporation is not planning to begin these selective, detailed reviews until after it issues commitment letters to applicants and their vendors informing them of the amount of funding that will be set aside to cover discounts for the services they are requesting. Should these subsequent reviews reveal systemic problems with the Corporation's quality assurance procedures or defects in the reviewed applications, the Corporation could find it difficult to take corrective actions since the commitment letters are, in essence, "green light" signals to the applicants and vendors to go ahead with the contracted services. If the Corporation finds major problems with some of the applications at this time, it may have to reduce or withdraw funding commitments previously made. These applicants might find themselves responsible for paying more of the cost of services received than they planned for.

Program Relies Heavily on Self-Certification

On the basis of the Joint Board's recommendations, FCC's orders specified that the application process for schools and libraries would be grounded on self-certification by applicants. This was done in the belief that the administrative burden on applicants should be limited, while still holding them accountable for the information they provide.

Accordingly, a responsible official must sign the application, certifying that the information presented is correct. FCC can impose civil and criminal penalties for applicants making willfully false statements. In addition to this general self-certification that all of the information provided is accurate, each application requires specific self-certifications about certain information provided. For example, the "request for services" application (FCC Form 470) requires applicants to self-certify that they or the entities they represent are an eligible school or library and that all services for which discounts are requested will be used for educational purposes only. The "request for discounts" application (FCC Form 471) includes additional self-certifications, such as assurances that all applicable state or local laws or rules regarding procurement have been followed. The applicants must also self-certify they have the budgetary

resources, not only to pay their share of the costs of requested services, but also those resources necessary to use and maintain the technology services for which discounts are requested.

In addition to the self-certifications on the Form 470 and Form 471 applications, FCC requires applicants to have a separate technology plan that provides details on how they intend to integrate technology into their educational goals and curricula, as well as how they will pay for the costs of acquiring and maintaining the technology. FCC requires that the plans be independently approved. To implement this requirement, the Corporation designates third parties, such as state education and library agencies or private school associations, to review and approve the plans on the basis of criteria provided by the Corporation. The schools and libraries do not routinely submit copies of their technology plans for review by the Corporation.

These technology plans do not have to be approved when the applications are submitted or even when the Corporation commits funding support to the applicants. However, the applicants must certify to the Corporation that their plans have been approved before any funds are disbursed to cover the services requested.

As a result, most applicants' requests for discounted services are not routinely reviewed by the third-party reviewers in order to determine whether, in fact, the requested services are linked to the educational goals described in the applicants' approved plans. According to Corporation officials, the third-party reviewers approve the plan but are not required to review the application. And, as noted above, the Corporation receives the application but does not routinely receive copies of the technology plan, although it may do so if it selects the application for a detailed review, as discussed below.

Issues Concerning Program Integrity Tests

The Corporation recognizes that self-certification and third-party approvals alone are not adequate controls to ensure compliance with the program's rules. It has therefore established a program integrity assurance operation that is designed to help ensure that applications and invoices submitted to the Corporation are complete, accurate, and in compliance with FCC's rules.

No program integrity tests are applied to the initial application for services (Form 470). Instead, the Corporation focuses on reviewing the information

submitted by applicants in their subsequent application for discounts (Form 471). The Corporation's review of this application takes place in two stages. During the first stage, when the Form 471 application is submitted to the Corporation's contractor, it is reviewed to ensure that it has met minimum processing standards. This review includes checking to see that the application has been signed by an authorized official and that the applicant is clearly identified. If the application does not meet the minimum standards, it is rejected and returned to the applicant. If the application meets minimum standards but is in some way unclear, it undergoes a "problem resolution" process, during which the Corporation's contractor contacts the applicant to ask for clarification.

At the second stage of the review process, the Corporation electronically compares information provided by the applicant against information in databases that the Corporation has compiled or purchased. Specifically, the Corporation runs three computer-assisted tests on each application. The set of tests: (a) compares the name of the applying school or library to a database of eligible schools and libraries, (b) looks for indications of whether any discounts are being requested for ineligible services, and (c) compares the discount requested by the applicant to the appropriate discount, as calculated from data maintained by the Corporation. Should these tests indicate potential problems with the eligibility of applicant, the eligibility of the services, or with the appropriateness of the discount, the Corporation's contractor contacts the applicant to resolve the issues identified. Depending on the additional information provided by the applicant, the application can be approved, revised, or rejected (in total or in part). Of about 20,000 applications entered into the database and tested as of July 7, 1998, roughly 14,000 were identified by at least one of the three tests as needing further review.

As indicated above, the Corporation has already applied these three tests to more than one-half of the 32,600 applications it has received. However, the Corporation added new criteria on several occasions to improve the particular test used to identify potentially ineligible services. Specifically, it added several criteria related to services prohibited under FCC's rules after a number of applications had already been reviewed. As a result, different test standards have been applied to the applications already processed, depending on when they were reviewed. According to Corporation officials, they do not plan to use the updated criteria to recheck applications processed earlier to determine if any passed that should have been flagged for problem resolution.

Another concern is the latitude of deviation allowed by the Corporation's automated test that checks whether an applicant is requesting an appropriate discount level. This automated test compares an applicant's requested discount with the appropriate discount as calculated from data in the Corporation's database. The Corporation is not reviewing all the applications showing discrepancies between the database calculation and the applicant's requested discount. Instead, it is allowing for a degree of deviation from the criteria established by FCC because, according to Corporation officials, the database used to conduct the test has some reliability problems. They are also concerned that reviewing all applications with any amount of deviation would increase processing time and costs without resulting in commensurate benefits.

We recognize that internal controls should provide reasonable, but not absolute, assurance of deterring or detecting noncompliance with laws, regulations, and management policies. However, part of determining the reasonableness of controls involves assessing them in relation to the associated risks, costs, and benefits. A key risk in this instance is that allowing inappropriately high discount levels to some applicants reduces the amount of discount support available for others. To date, the Corporation has not performed a benefit-cost analysis to justify that its approach is reasonable. Specifically, the Corporation has not determined the total dollar amount of potentially inappropriate discounts that is passing unchallenged through its computer-based test.

In addition to the tests described above, the Corporation plans to conduct other computer-assisted tests on the applications. For example, it plans on testing for duplicate applications. However, these tests have not been finalized.

Detailed Review of Applications Not Planned Until After Funds Are Committed

In addition to these computer-assisted tests, the Corporation plans to conduct more detailed manual reviews of applications that it considers to be "high risk." However, according to current plans, these reviews will not be performed until after funds are committed to applicants and vendors.

To carry out these detailed reviews, the Corporation will designate applications as high risk if they (1) request a large total amount of funds, (2) request a large amount of funds compared with other applications on a per-unit basis (such as per-student or per-patron), (3) are from wealthy

private schools,[7] or (4) have been placed on an "alert list" of applications that have been identified in some way as potentially violating the program's rules. Although the procedures for these detailed reviews have not been finalized, the Corporation plans to require applicants to submit additional material to support the information provided in their applications, such as technology plans, budget information, requests for proposals, and bids. Using this material, the Corporation staff will give these high-risk applications a detailed review for compliance with the program's rules, such as those regarding eligibility of services and prohibitions against the improper consideration of "free services" in awarding contracts.

Performing these reviews after commitment letters have been sent has some disadvantages. First, the reviews would not help the Corporation evaluate the effectiveness of its three automated compliance tests before funds are committed. As a result, it may not be able to identify and correct any systemic problems in its application review process prior to commitment. In addition, if the Corporation finds major problems at this time with the applications reviewed, it may have to reduce or withdraw funding commitments from applicants. This could cause problems for applicants that have begun receiving services on the basis of their commitment letters. These applicants might find themselves responsible for paying a higher cost for those services than they planned.

Key Program Procedures Have Not Yet Been Finalized

The Corporation has not yet finalized all the procedures, systems, and internal controls that it needs in order to make funding commitments and approve vendor compensation for the discounted services provided to applicants. Corporation officials stated that some progress has been made in developing the procedures and controls needed to conduct these processes and in developing the automated systems needed to carry them out. However, the procedures are still subject to change. In fact, key control documents in this process—the commitment letters and the "Receipt of Service" form (FCC Form 486) which triggers the funds disbursement process — have yet to be made final. Corporation officials could not estimate when these procedures and forms would be finalized.

This situation is of concern because these procedures could be needed very shortly after commitment letters are sent to applicants and vendors. For example, applicants who are already receiving eligible services under

[7]Under the Telecommunications Act of 1996, private schools with endowments of more than $50 million are not eligible to participate.

existing contracts could quickly send in their Form 486s for processing once they receive commitment letters. Similarly, their vendors could quickly begin submitting invoices, and the Corporation could begin processing them once the related Form 486s have been accepted. The Corporation itself estimates that the invoices for payment could begin as soon as 15 days after commitment letters are sent. If the procedures and internal controls for this phase of the program are not in place when commitment letters are issued, the Corporation may find itself unable to process vendor invoices in a timely manner.

According to Corporation officials, the delay in finalizing the commitment letters and disbursement procedures is due to the priority they have given to processing the backlog of applications as well as to anticipated changes in the program's rules. As discussed earlier, FCC made changes to the universal service program in June 1998.[8] As described in the order, there were two primary changes to the schools and libraries discount program. First, the funding year was changed from a calendar year to a fiscal year, effective immediately. To ease the transition, the 1998 funding year was extended 6 months to end June 30, 1999. According to FCC, this change was made because delays in starting the program made it difficult for some schools to use the funds within the original time period and because a fiscal year calendar is more convenient for applicants and for the companies that pay for universal service.

Second, the order changed the funding priorities for schools and libraries. Previously, FCC rules did not provide for any differentiation among applications that were received during the initial 75-day application window, except to specify that the last $250 million would be distributed on a priority basis to the applicants eligible for the highest discount levels. However, after recognizing that the funds provided by its orders would probably not cover all of the applicants' requests, FCC changed its priority rules so that all applications for telecommunications and Internet services would be funded first. The remaining funds would be distributed to applicants asking for internal connections, and those with the highest discount levels would be funded first. Corporation officials stated that they are still developing procedures to implement these changes, including procedures to allow applicants to amend their applications.

[8]Fifth Order on Reconsideration and Fourth Report and Order in FCC Docket No. 96-45, FCC 98-120, released June 22, 1998.

Verification of Soundness of Internal Controls Not Planned to Be Completed Before Funds Are Committed

In December 1997, FCC's Chairman requested the Corporation to contract with an independent auditor to verify that the program's processes and procedures provide the controls needed to mitigate against fraud, waste, and abuse. The Corporation accordingly engaged the services of an independent audit organization, which is currently reviewing the Corporation's systems and procedures and providing advice on improvements. According to current plans, the auditor's report is due to be completed before the Corporation authorizes the disbursement of funds.

The independent audit is to include a review of the design of the program's integrity assurance operations. According to the Corporation, the audit objectives are to determine if the Corporation has designed the controls necessary to provide reasonable assurance that (1) all applications are processed in the order received; (2) only eligible schools and libraries receive discounts for eligible services; (3) the discount percentages are calculated in accordance with FCC's orders; (4) payments for reimbursements to vendors are timely; and (5) funding commitments do not exceed the program's limits. However, the Corporation stated that these control objectives have not been finalized and are subject to change.

The auditor's scope of work, in this start-up phase, is focused on the design of the controls and will not include a verification of how effectively the controls have been applied. For example, the auditor will not review a sample of applications to determine whether the eligibility tests for applicants and services actually identified the applications that could have compliance problems.

We believe that the independent audit can be useful in strengthening the program's integrity, even with its limited scope of work. We are concerned, however, about the timing of the auditor's final report, which is not due until after funding commitment letters have been issued to applicants and vendors. When we discussed our concern with Corporation officials, they proposed having the auditor brief the Corporation's Board of Directors on its preliminary results regarding "pre-commitment" procedures before the Corporation sends out funding commitment letters.

This approach, however, does not adequately address our concerns. The briefing would not cover the procedures that the Corporation would use for its post-commitment review of applications that it designates as high risk. More important, the briefing would not cover the procedures, systems, and internal controls associated with disbursing funds. As noted earlier, applicants and vendors could begin sending in forms and invoices

for funds disbursement as soon as 15 days after commitment letters have been sent out. It is therefore important that the Corporation have all of its disbursement procedures, systems, and controls in place and reviewed by the independent auditor before commitment letters are issued. If the auditor's final report comes later and identifies problems with disbursement procedures, it may be difficult for the Corporation to resolve them in a timely manner so that vendor invoices can be processed promptly and accurately. Currently, the Corporation does not know when the auditor's formal report will be completed, partly because it does not know when it will finalize the funds disbursement procedures, systems, and controls for the auditor to review.

Program Lacks Clear and Specific Performance Goals and Measures

Performance measurement is critical to determining a program's progress in meeting its intended outcomes. Accordingly, the Congress, FCC, and the Corporation need clearly articulated goals and reliable performance data to assess the effectiveness of the schools and libraries program.

FCC's combined "Strategic Plan for Fiscal Years 1997-2002 and Annual Performance Plan for Fiscal Year 1999," prepared in response to the Results Act, mentions the schools and libraries program in the context of a large number of telecommunications initiatives. However, this document provides no specific strategic goals, performance measures, or target levels of performance for the program as required by the act.

The schools and libraries program is listed under the combined plan's "Policy and Rulemaking Activity Objective 2," which states that FCC "will encourage competition in the telecommunications industry through pro-competitive, deregulatory rulemakings, reducing consumer costs and increasing the telecommunications choices available to consumers." However, this is a high-level, comprehensive goal that includes a wide array of telecommunications initiatives, such as radio spectrum management, the allocation of toll-free numbers, the review of merger requests, and standard setting for global communications services. Moreover, for all of the varied activities under this goal, there is a single general performance indicator: "Performance will be measured by an annual compilation of the number of actions taken by the Commission to promote competition and an analysis of the result of these activities on consumers." While enhancing competition is part of FCC's mission, it is not clear how this statement translates into a strategic goal for the schools and libraries program.

Similarly, the annual performance goal for the schools and libraries program in fiscal year 1999 is too general, stating simply that FCC "will work to improve the connections of classrooms, libraries and rural health care facilities to the Internet by the end of [fiscal year] 1999 and to maintain affordable Telecommunications services to rural America." FCC needs to make the performance goals and measures for the program more specific to bring them in line with the Results Act's requirements. The act defines an annual performance goal as the target level of performance expressed as a tangible, measurable objective against which actual achievement is to be compared. An annual performance goal is to consist of two parts: (1) the performance measure that represents the specific characteristic of the program used to gauge performance and (2) the target level of performance to be achieved during a given fiscal year for the measure.

According to Corporation officials, they have begun exploring options for performance measurement. For example, they have identified a number of existing data sources that could be used to develop baseline data and measure trends in areas such as Internet connections. While this is encouraging, it is important that FCC take the lead as part of its policy-making and oversight responsibilities for the program. FCC can build on the Corporation's preliminary work in revising its own annual performance plan to define specific goals and measures for the program. GAO has issued guidance on developing effective strategic plans which FCC should find useful.[9]

Conclusions

We recognize that a program in its first year of operation faces many challenges and difficulties. While the initial year cannot be expected to unfold without any problems, it is important that the program's managers identify the major risks facing the program and address them at the time when corrective actions would be most effective. This time is approaching for the Corporation as it prepares to issue its first set of funding commitment letters to successful applicants. Given our concerns over the program integrity assurance operations, we believe that the Corporation needs to complete additional actions before, rather than after, commitment letters are issued to applicants. Waiting until after commitment letters have been issued will make it difficult for the Corporation to take effective actions to correct any systemic problems in the application review procedures and could put the Corporation in the

[9]See Executive Guide: Effectively Implementing the Government Performance and Results Act (GAO/GGD-96-118, June 1996) and Agencies' Strategic Plans Under GPRA: Key Questions to Facilitate Congressional Review (Version 1, GAO/GGD-10.1.16, May 1997).

position of having to withdraw funding commitments from applicants, even those who have begun receiving services from vendors. Similarly, issuing commitment letters before all of the program's operating procedures, systems, and internal controls have been finalized and verified (especially those dealing with authorizing the disbursement of funds) would put the program's integrity at risk.

Recommendations

To help strengthen the Corporation's program integrity assurance operations and help ensure that funding is properly directed to eligible applicants, for eligible and appropriate services, and at appropriate discount levels, we recommend that the FCC Chairman direct the Chief Executive Officer of the Schools and Libraries Corporation to complete the following actions before issuing any funding commitment letters to applicants:

- Conduct detailed reviews of a random sample of applications to assess not only the soundness of these applications but also the overall effectiveness of the Corporation's program integrity procedures for detecting ineligible applicants, ineligible services, and inappropriate discount levels as defined by FCC orders. Should these reviews reveal systemic weaknesses in program integrity procedures or their implementation, the Corporation should take corrective actions before committing any funds.

- Finalize procedures, automated systems, and internal controls for the post-commitment phase of the program's funding cycle, including funds disbursement.

- Obtain a report from its independent auditor that finds that the Corporation has developed an appropriate set of internal controls to mitigate against waste, fraud, and abuse.

In addition, before issuing commitment letters for those applications identified as "high risk," the Corporation should conduct detailed reviews of the technology plans and related documents to determine whether the applicants have the resources to effectively use the services requested and whether the applications are in compliance with FCC rules regarding eligibility.

Finally, we recommend that the FCC Chairman direct responsible FCC staff to develop goals, measures, and performance targets for the schools and

libraries program that are consistent with the requirements of the Results Act. These measures should be defined by the end of this Federal fiscal year so that data collection and analysis activities can begin during the program's first funding cycle and goals can be communicated to future applicants.

Scope and Methodology

We performed our review during June and July 1998 in accordance with generally accepted government auditing standards. We met with officials from FCC and the Corporation to review the progress being made in starting up the schools and libraries program and implementing the first year's funding cycle. We also met with the Corporation's contractor in New Jersey, which has major responsibilities for processing and reviewing the program's applications. We reviewed guidance and procedures developed by FCC and the Corporation, along with status reports on the program's activities and cost data. We did not verify the accuracy of the information in these reports or the cost data.

Agency Comments

We discussed our findings and recommendations with FCC and Corporation officials. The Corporation's Chief Executive Officer agreed with our recommendations. In addition, in response to Corporation comments, we made a few revisions including clarifying the scope of the detailed compliance reviews. FCC's Common Carrier Bureau Chief stated that the recommendations are reasonable.

Mr. Chairman, this concludes our testimony. We would be happy to answer any questions that you and members of the Committee may have at this time.

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